



The Conference Board

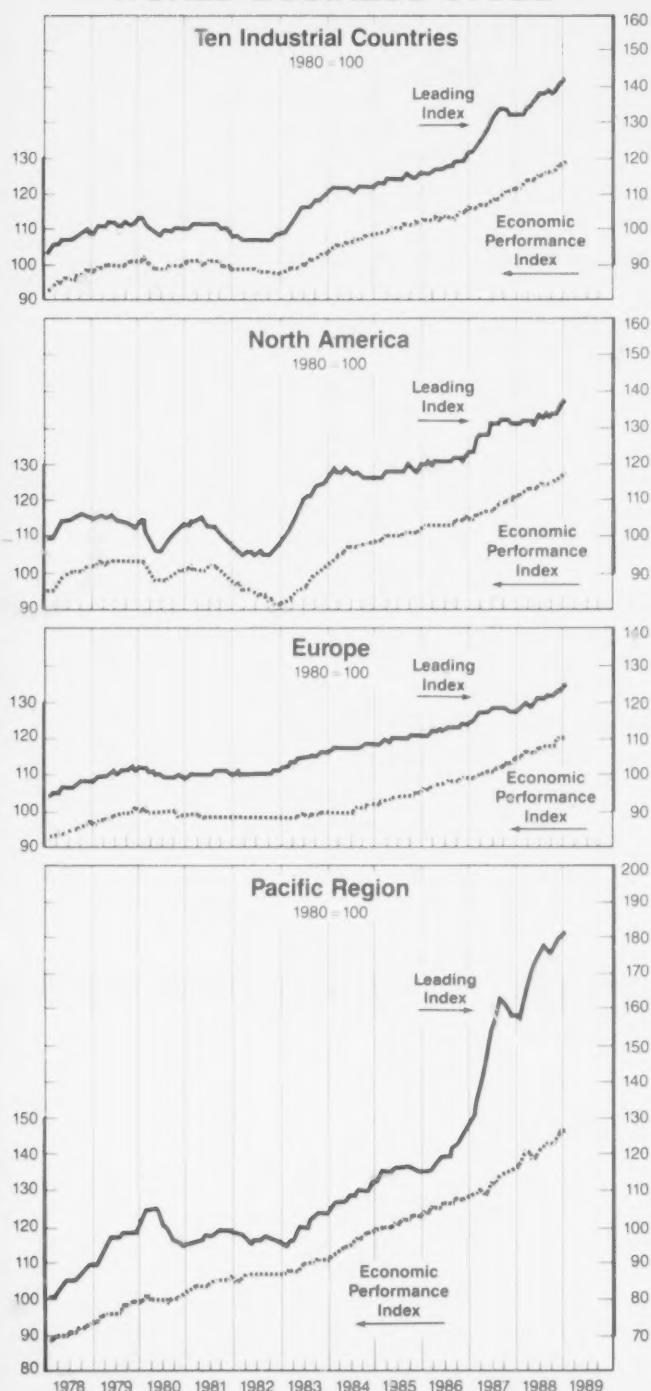
Economic and Business Environment Program

International Economic Scoreboard

A Quarterly Report from The Conference Board

Second Quarter 1989

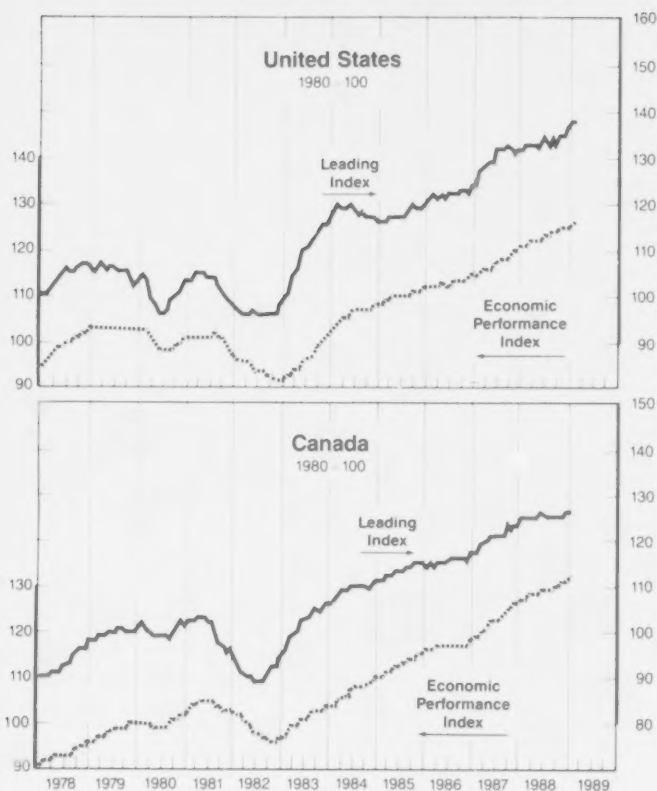
WORLD BUSINESS CYCLE



The business cycle indexes for the world's major industrial countries have been advancing so steadily and so persistently that it's hard to get interested in another round of good news. But that's what we've got, and it can't be discounted. The 10-country leading index is growing at 8 percent, the highest reading in more than a year. Furthermore, every growth rate shown in the Summary Table (p.2) is a positive number, and of the latest numbers all but one (Canada's leading index) show a respectable pace of advance.

Once again, the Pacific Region is experiencing the greatest exuberance, with a growth rate for the leading index that's twice as fast as North America and Europe. Among individual countries, Japan leads the parade with a rousing 13 percent growth rate. Other nations with strong expansion signals are Taiwan (9 percent), South Korea and France (each 8 percent) and West Germany (7 percent). The only possible question marks are Canada, where the leading index has been flat for a year, and Australia, where the leaders have been flat for about half a year.

NORTH AMERICAN COUNTRIES



The leading index for the United States continues to move upward, with higher materials and common stock prices leading the way. The latest growth rate is a more-than-respectable 6 percent. With the economy operating so close to capacity, inflation is much more of an immediate threat than recession.

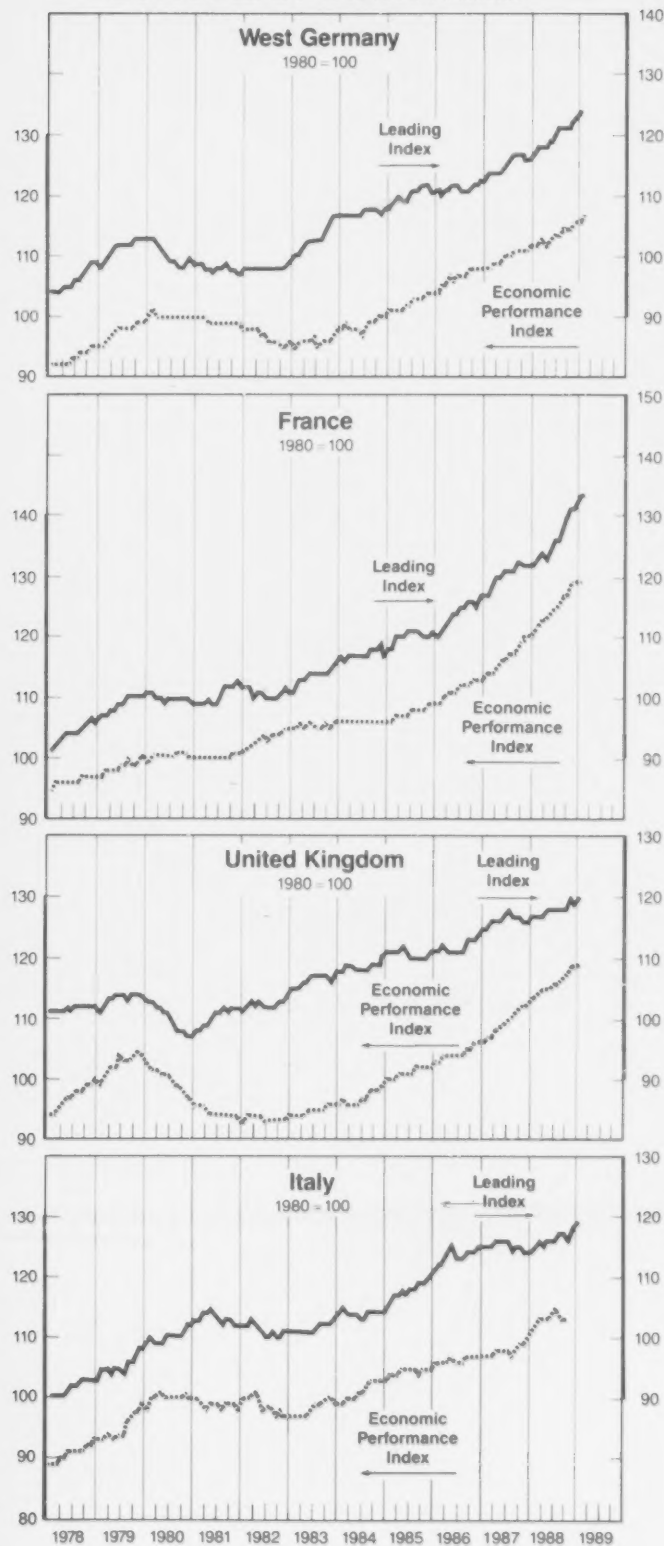
The Canadian economy continues to move ahead on its long expansion path, despite the indecisive trend of the leaders. Among the component leading indicators, the two new orders series—for consumer goods and for machinery and equipment—have contributed the most weakness to the composite index in recent months.

Summary Of Growth Rates, Ten Industrial Countries

	Ten-year Growth Rate	Indexes of Economic Performance Growth Rates*			Leading Business Cycle Indexes Growth Rates*			Current Reading on the Cycle	Latest Month Covered
		6 mos. ago	3 mos. ago	Latest month	6 mos. ago	3 mos. ago	Latest month		
		annual rates, percent							
Ten countries	3	5	5	5	6	5	8	Expansion continuing	Jan.
9 countries excl. U.S.	3	6	5	5	9	7	9	Expansion continuing	Jan.
North America (2)	3	5	4	5	1	3	6	Expansion continuing	Jan.
Europe (4)	2	5	4	5	4	5	7	Expansion continuing	Jan.
Pacific Region (4)	4	7	7	6	15	10	12	Expansion continuing, leaders strong	Jan.
United States	3	4	4	6	3	3	4	Expansion continuing	Feb.
Canada	3	5	4	4	1	0	1	Expansion continuing, leaders weak	Jan.
West Germany	2	5	4	4	5	5	7	Expansion continuing	Feb./Jan.
France	2	7	6	7	6	9	8	Expansion continuing	Jan./Feb.
United Kingdom	2	5	6	5	2	2	3	Expansion continuing	Jan.
Italy	2	7	7	2	2	3	5	Expansion continuing	Oct./Jan.
Japan	4	7	6	5	16	11	13	Expansion continuing, leaders strong	Jan.
Australia	3	8	11	10	8	4	2	Expansion continuing	Jan.
Taiwan, R.O.C.	8	8	10	7	17	14	9	Expansion continuing	Feb.
Korea, R.O.K.	7	8	6	8	13	10	8	Expansion continuing	Feb.

* Ratio of current month's index to average index over the preceding 12 months, expressed as a compound annual rate.

EUROPEAN COUNTRIES



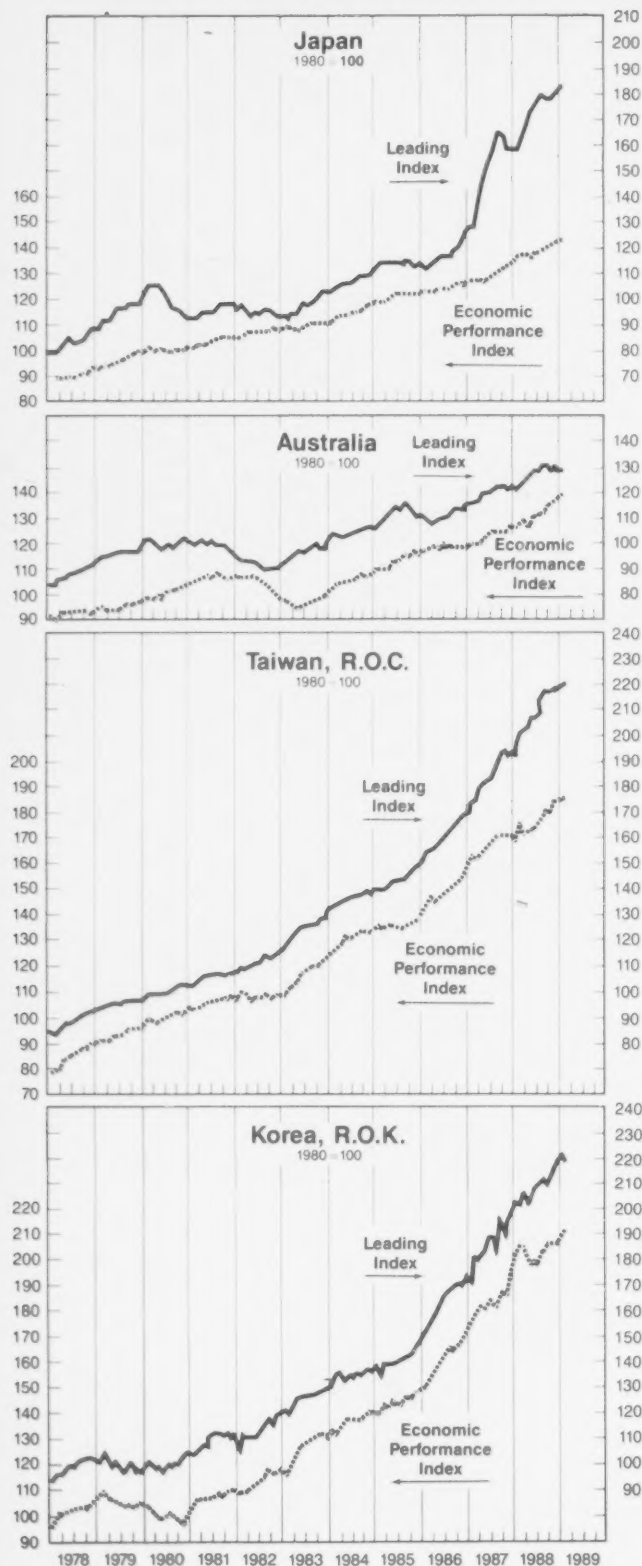
In West Germany, the business cycle shows the same persistent advance as is seen in the rest of the industrial world. Since our last report the outlook has strengthened somewhat, with the leading index showing a solid 7 percent growth rate, up from 4 percent three months ago. The acceleration of the leaders was paced by materials prices and common stock prices.

The French economy is the most robust in Europe these days. The performance index is advancing at a 7 percent rate, and the leading index at a spirited 8 percent.

Prospects for the U.K. economy have improved. At the time of our previous report, the leading index was weak (declining at a 1 percent rate). That figure has now been revised to a 2 percent growth rate, and the latest is a more adequate 3 percent growth rate. Consequently, the caution expressed last time about chances the upswing would not continue can be set aside again.

The Italian indicators (always thin and always late, and thus always tenuous) look a bit more encouraging this time. The leading index, which was rising at a 3 percent rate three months ago, now registers a more sturdy 5 percent growth rate.

PACIFIC REGION COUNTRIES



The Japanese statistics continue to set the pace for the industrial world. The overall growth rate of the economy is an unremarkable 5 percent, but Japan's leading index is climbing at a 13 percent pace. Thirteen percent is not all that unusual a rate for Japan, but coming as it does after a phenomenal climb of more than two years duration (see top line on accompanying chart) it is an impressive number.

In Australia, the economy continues to advance briskly. Since last June, however, the leading index has cooled off, especially materials prices and common stock prices. The movement of those two price series represents a puzzling contrast to the rest of the industrial world, where both materials and stock prices have been climbing almost without exception. (Is that why it's called "down under"??)

The business cycle outlook for Taiwan, R.O.C., still looks very favorable. The performance index is advancing at a 7 percent rate, and the leading index at 9 percent, both very solid (although not-out-of-the-ordinary) numbers for this country.

The economic outlook for South Korea, R.O.K., is almost a twin to Taiwan's. Both of South Korea's indexes show a growth rate of 8 percent, not outstanding for this newly industrializing country, but encouraging nonetheless.

U.S. TRADE WITH EUROPE: THE GOOD NEWS AND THE BAD NEWS.

The good news about the trade balance in January was that the U.S. ran a slight trade surplus with Western Europe, the first American trade surplus with that area in more than five years. The U.S. deficit with the United Kingdom in December became a surplus in January, the deficit with West Germany was nearly halved and there was a small surplus with France. The Commerce Department's report on the reduction in the overall trade deficit and the small surplus with the European Economic Community had favorable effects on the dollar as well as on stock prices. However, one swallow does not make a summer. How lasting is this change? Will the improvement carry on through 1989, or are these January numbers an aberration?

The Scoreboard's leading indicators can help to answer this question. Our leading index for Europe covers the four major countries: France, West Germany, Italy, and the United Kingdom. That index should tell us about the prospects for U.S. exports to those areas. The index was, of course, designed to lead movements in business activity in Europe, specifically to tell us when business there is about to pick up or to slow down. Such movements obviously affect U.S. exports. Similarly, the U.S. leading index bears on the outlook for U.S. imports, including those from Europe. In addition, the decline in the dollar's exchange rate of 40 percent against the D-mark, 33 percent against the franc, 31 percent against the lira, and 28 percent against the pound from 1985 through the end of 1988 has had a positive impact on U.S. exports. It turns out, however, that the dollar's decline has had little or no impact on U.S. imports from Europe.

When these relationships are assembled into a couple of forecasting equations, they work pretty well. Year-to-year growth in U.S. exports to Europe is forecast, as shown on the first chart, using the growth rate in the European leading index as of the preceding September and the growth rate in the dollar exchange rate as of the preceding July. For 1989 the forecast calls for a 13 percent gain. Correspondingly, U.S. imports from Europe are forecast, as shown in the second chart, using the preceding September growth rate in the leading index for the U.S. economy. For 1989 this relationship forecasts an 11 percent increase in U.S. imports from Europe.

We then use the results from the first two relationships to calculate the forecast and actual U.S. trade balance with Europe for the years 1978 through 1989. The forecast values are derived from the estimated percent changes in U.S. exports and imports in Charts 1 and 2, converted to dollar amounts. As Chart 3 discloses, the relationship between the forecast and actual balances is a very close one. In fact, the correlation coefficient (r^2) is 97 percent.

What does this tell us about 1989? Here the news is not so good. The forecast 11 percent increase in U.S. imports from Europe, expressed in dollars, more than matches the forecast 13 percent increase in U.S. exports to Europe. Hence we should expect a further small increase in our trade deficit with Europe, some \$32 billion in all. In other words, the bad news is that the good news reported for January probably was a fluke.

THE INTERNATIONAL ECONOMIC INDICATOR SYSTEM

This publication is designed to help readers monitor the ups and downs of the business cycle around the world. To this end, two types of index are shown for each country: an index of economic performance and a leading index. The economic performance indexes are composites of such series as real GNP, industrial production, employment and sales—what analysts call “coincident” series, because they define the business cycle.

The leading indexes are composites of such series as new orders, construction contracts, corporate profits and stock prices—indicators that usually anticipate changes in production and employment by several months. Thus, the indexes of economic performance tell us the current status of the business cycle, i.e., where we are, while the leading indexes tell us where the economy is headed.

Experience has shown that when the leading index begins to rise faster, it is a fairly safe rule that the economy will soon begin to rise faster too—typically after three or four months. When the leading index begins to rise more slowly or to decline, the economy is likely to follow suit shortly thereafter. (For details, see “What the Leading Indicators Indicate,” *Across The Board*, April 1980 and *Business Cycles, Inflation and Forecasting*, Ballinger Publishing Co., 1983.) Considerable variation in the length

of the lead is to be expected, however. Constant monitoring is needed to make effective use of the system and to get early warnings of recessions and recoveries, changes in foreign trade flows, and new inflationary trends.

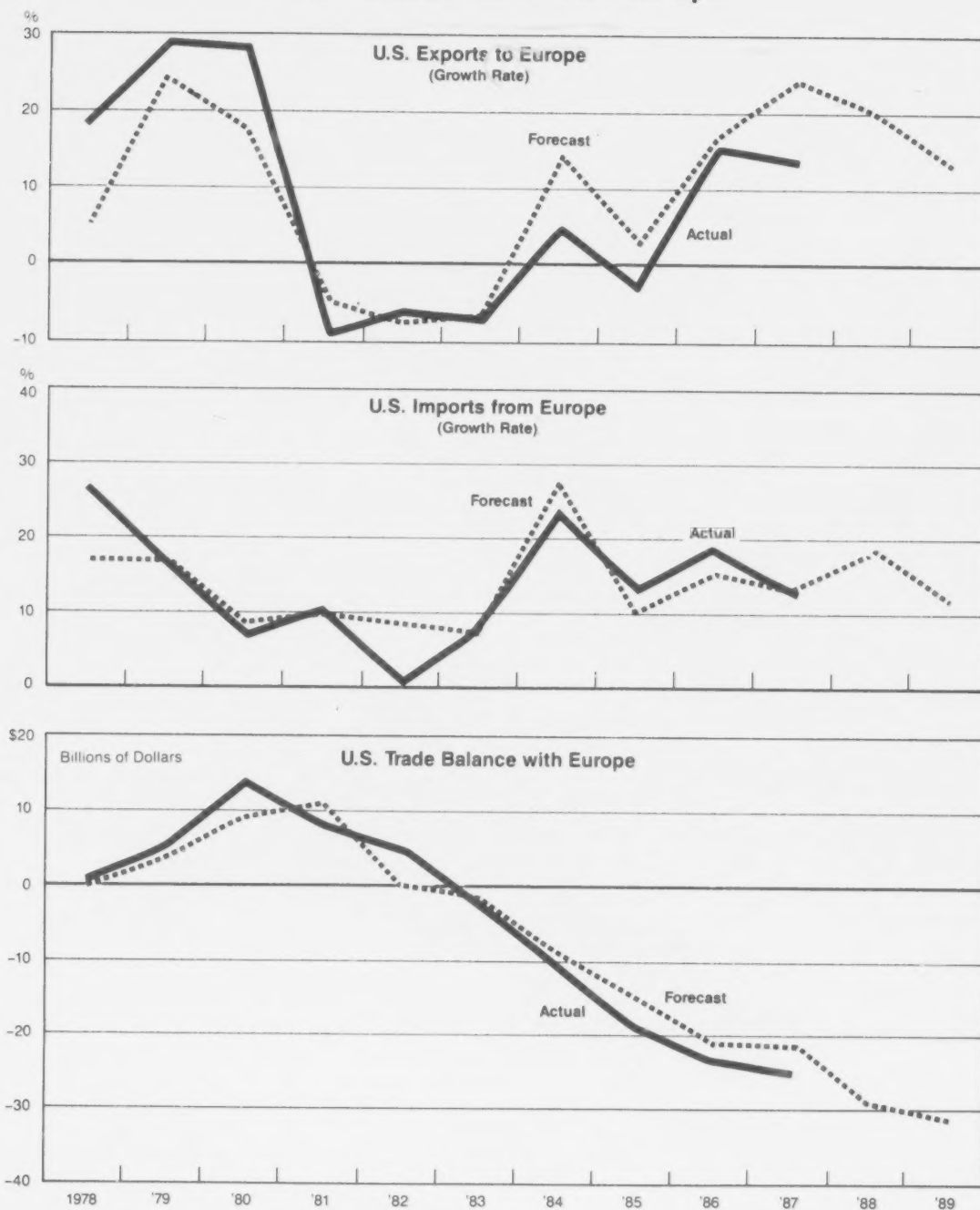
The indexes were developed by Geoffrey H. Moore and Philip A. Klein, and are maintained by the Center for International Business Cycle Research at the Columbia Business School. (The U.S. indexes used here differ slightly from the indexes reported monthly by the U.S. Dept. of Commerce.) To facilitate analysis the indexes are adjusted so their long-run growth rates are equal to those in real GNP in the country concerned. These growth rates are shown in the first column of the table on page 2 of the quarterly version of the *Scoreboard*.

For More Information

To find out more about this indicator system and the availability of detailed data for each country please address inquiries to:

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United States Trade with Europe



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